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U.S.-Japan Currency Agreement Includes Cut In Japan's Discount Rate

In an October 31 agreement between the United States and Japan, Washington agreed to end its pressure for a stronger yen in exchange for more stimulative economic policies by Tokyo. The accord stated that "the exchange rate realignment achieved between the yen and the dollar since the Plaza agreement is now broadly consistent with the present underlying fundamentals." Recognizing the threat of currency instability to economic growth, the two sides agreed "to cooperate on exchange market issues." Some observers interpreted this as the establishment of a de facto target zone that will be maintained by joint intervention. Although it stated that measures by other industrial nations are critical to promote world growth, the agreement did not include the European countries.

Government Submits Supplementary Budget To Diet

Tokyo's long-awaited FY 1986 supplementary budget was sent to the Diet October 31 to implement the economic stimulus package announced September 19. The budget calls for a Y549 billion ($3.5 billion at Y155=$1.00) issue of construction bonds to fund public works (see Table). Finance Minister Kiichi Miyazawa said the government has done its best to stimulate the economy, given the fiscal constraints it faces.

FY 1986 Supplementary Budget*

(in billions of yen)

Expenditures	Amount
Public Works	Y549.0
General Public Works	133.0
Disaster Relief Projects	416.0
Incentives for Private-Sector Investment	3.3
Small and Medium Business Programs	25.2
Civil Service Wage Increases	133.8
Fishing Industry Adjustment	19.6
Transfer from National Bond Redemption Fund	-410.0
Transfer to Special Oil Account	-54.0
Transfers to Local Governments	-450.2
Unused Funds	-452.0
National Bond Interest Payment Fund	-253.8
Fuel Fund	-74.0
Reserve Fund	-150.0
Other	521.5
Total	-263.8

Revenue	Amount
Taxes	Y-1,120.0
Income	-426.0
Corporate	-981.0
Oil	-205.0
Tariffs	-75.0
Inheritance	219.0
Securities Transfer	348.0
Non-Tax Revenue	-133.4
Bank of Japan Contribution	-197.9
Construction Bonds	549.0
Budget Surplus from FY 1985	440.5
Total	-263.8

*Change from the initial general account budget passed in April 1986.

Source: Nihon Keizai Shimbun, October 28, 1986

The Y3.6 trillion ($23.2 billion) stimulative package adopted by the cabinet in mid-September is designed to help the economy achieve the government's outlook of 4 percent real growth in FY 1986. Its key component is Y1.4 trillion ($9 billion) in additional public works spending. Of this total, Y602 billion ($3.9 billion) will be financed in future budgets and Y243 billion ($1.6 billion) will be handled by local governments, leaving Y549 billion to be funded by this year's supplementary budget. The stimulus package also includes Y800 billion ($5.2 billion) in regional projects to be financed by local governments; higher loan ceilings for the Housing Loan Corp. to induce an additional Y700 billion ($4.5 billion) in housing construction; and Y100 billion ($645 million) in road construction to be financed under the Fiscal Investment and Loan Program. The government is also projecting Y360 billion ($2.3 billion) in additional private-sector investment by electric and gas utilities and Kokusai Denshin Denwa Co., Ltd., Japan's international common carrier.

Because of the slowing economy, the Ministry of Finance anticipates revenue in FY 1986 to fall Y1,253 billion ($8.1 billion) short of its original projections (see JEI Report No. 1B, January 10, 1986). Tax revenue, projected to rise 6.2 percent, was up only 0.2 percent in August from a year earlier. Smaller-then-expected summer bonuses and cutbacks in overtime work have slowed the increase in individual earnings, and revenue from corporate taxes has dipped substantially, reflecting the effect of the strong yen on business activities. Oil tax revenue is down due to the drop in oil prices, while cheaper import prices and lower tariff rates have cut customs revenue.

In line with its goal of ending reliance on deficit-covering bonds by FY 1990, the government plans to cover this fiscal year's expected revenue shortfall with Y441 billion ($2.8 billion) in reserves carried over from FY 1985 and with savings in other expenditures. Lower oil prices will limit expenses in many areas, particularly defense. Moreover, falling interest rates have reduced the cost of financing the national debt. As a result of these savings, FY 1986 government expenditures will be Y263.8 billion ($1.7 billion) below the original budget, despite increased outlays on public works (see JEI Report No. 11B, March 21, 1986).

Randall S. Jones

Japanese Firms Enlarge Wall Street Presence

The trend toward integration of national financial markets was highlighted recently when the Industrial Bank of Japan, Ltd. announced that one of its subsidiaries was poised to purchase an elite U.S. securities broker. The move, along with an agreement between Sumitomo Bank, Ltd. and Goldman, Sachs & Co., underscores the drive by Japanese firms to establish a strong presence in American financial markets. This has generated some grumbling by American competitors that claim that reciprocal opportunities are not available for U.S. firms in Japan. While federal authorities do have the power to block both agreements, approval is likely.

Sumitomo Bank first stirred the waters on August 6 by confirming rumors that it was negotiating a limited partnership arrangement with Goldman, Sachs, one of Wall Street's largest privately held investment bankers. The third-largest Japanese commercial bank (with assets of Y32.2 trillion -- $207.7

Trade and Payments Data
(in millions of dollars unless otherwise indicated)

	1984	1985	January-September 1985	January-September 1986	July 1986	August 1986	September 1986
Japan's Balance of Payments							
Trade Balance	$44,257	$55,986	$38,207	$65,053*	$8,666*	$8,114*	$9,799*
Exports (f.o.b.)	168,290	174,015	124,872	150,963*	18,514*	16,627*	18,739*
Imports (f.o.b.)	124,033	118,029	86,665	85,910*	9,848*	8,513*	8,940*
Current Account Balance	35,003	49,169	33,175	59,953*	8,026*	7,054*	9,106*
Long-Term Capital (net)	-49,651	-64,542	-45,830	-86,427*	-11,958*	-13,162*	13,435*
Overall Balance	-15,200	-12,318	-9,085	-20,295	-629	-5,472	-3,872
International Reserves (end of period)	26,313	26,510	27,523	41,456	38,330	41,214	41,456
Japan's Customs Clearance Trade							
Trade Balance	33,611	46,099	30,315	58,746*	8,194	7,478	8,920*
Exports (f.o.b.)	170,114	175,638	126,160	153,433*	18,895	16,837	19,002*
Cars	21,899	25,402	17,845	24,437*	3,066	2,550	2,910*
Steel	13,852	13,566	10,023	9,450*	1,171	1,070	1,056*
Imports (c.i.f.)	136,503	129,539	95,846	94,687*	10,701	9,359	10,082*
Crude Oil	39,379	34,599	25,376	15,569*	1,075	1,076	1,030*
Japan-U.S. Trade							
Trade Balance	33,075	39,485	27,274	36,818*	4,515	4,416	4,805*
Exports (f.o.b.)	59,937	65,378	46,797	58,875*	7,490	6,498	7,258*
Imports (c.i.f.)	26,862	25,793	19,523	22,057*	2,975	2,082	2,453*
U.S.-Japan Trade							
Trade Balance (f.a.s./c.i.f.)	-36,796	-49,749	-36,938	-43,028	-5,505	-4,701	-4,120
Trade Balance (f.a.s./Customs)	-33,560	-46,152	-34,219	-40,340	-5,161	-4,422	-3,869
Exports (f.a.s.)	23,575	22,631	17,064	20,301	2,941	2,272	2,015
Industrial Supplies	9,139	8,680	6,468	6,281	624	725	810
Food and Feed	5,929	5,001	3,773	3,754	462	553	395
Capital Goods	5,627	5,939	4,490	4,815	650	588	555
Consumer Goods	1,476	1,416	1,093	1,239	143	168	138
Imports (Customs)	57,135	68,783	51,282	60,641	8,102	6,694	5,884
Automotive Products	18,477	24,980	18,197	24,116	3,525	2,734	2,129
Capital Goods	19,290	21,516	16,314	18,740	2,347	2,093	1,968
Consumer Goods	11,266	14,017	10,364	11,458	1,428	1,213	1,173
Industrial Supplies	7,276	7,035	5,504	5,339	676	543	509
Imports (c.i.f.)	60,371	72,380	54,002	63,328	8,446	6,973	6,136

*Preliminary

Japanese Economic Indicators

(percentage change from year-earlier period unless otherwise indicated)

	1984	1985	January-August 1985	January-August 1986	June 1986	July 1986	August 1986
Discount Rate (end of period)	5.0%	5.0%	5.0%	3.5%	3.5%	3.5%	3.5%
Outstanding Money Supply	7.8%	8.4%	8.1%	8.7%	8.5%	8.7%	8.9%
Industrial Production	11.1%	4.6%	6.2%	-0.3%	0.2%	-1.5%	-3.0%
Manufacturing Operating Rate	7.3%	1.2%	1.9%	-4.1%	-4.4%	-5.6%	-7.8%
Number of Bankruptcies	8.8%	-9.7%	-8.9%	-7.7%	-3.6%	-8.2%	-8.0%
Residential Construction Starts	4.4%	4.1%	3.6%	7.1%	4.7%	13.5%	19.4%
Job Openings to Applications (ratio)	0.65	0.68	0.69	0.63	0.60	0.61	0.61
Nominal Wages	4.3%	3.6%	3.9%	3.8%	4.8%	3.9%	1.6%
Labor Productivity	9.9%	4.2%	6.1%*	2.2%*	2.0%	n.a.	n.a.
Wholesale Prices	-0.3%	-1.1%	0.0%	-8.7%	-10.1%	-10.7%	-11.2%
Consumer Prices	2.3%	2.0%	2.3%	0.9%	0.6%	0.1%	0.1%
Yen-Based Export Prices	0.6%	-1.4%	2.0%	-15.9%	-16.5%	-17.5%	-17.8%
Yen-Based Import Prices	-3.4%	-2.5%	1.1%	-33.1%	-39.6%	-41.9%	-43.9%

*Through June of each year only.

For Japan's most recent GNP figures, see JEI Report No. 34B, September 19, 1986.

STATISTICAL SUPPLEMENT